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February 13, 1998

Greg Lipscomb, Esquire
Formal Complaints and Investigation Branch
Common Carrier Bureau
Federal Communications Commission
2025 M Street, N. W., Room 6120
Washington, D. C. 20554

97-237

Re: *AT&T Corp.* v. *Beehive Telephone Co., Inc.*,
File No. E-97-04

Beehive Telephone Co., Inc. v. *AT&T Corp.*,
File No. E-97-14

Dear Mr. Lipscomb:

It is my understanding that the Commission will consider the record of the access tariff investigation in CC Docket No. 97-237 when it decides the above-referenced consolidated complaint cases. Accordingly, I have enclosed for consideration three copies of the Petition for Reconsideration filed by Beehive Telephone Company, Inc. and Beehive Telephone, Inc. Nevada with respect to the Commission's *Memorandum Opinion and Order*, FCC 98-1 (Jan. 6, 1998) in the tariff investigation.

Please note that the copies of the petition have been corrected to conform to an erratum to the pleading that I filed on February 6, 1998.

Please give me a call should you have questions with regard to this matter.

Very truly yours,

Russell D. Lukas

cc w/encl.: Peter H. Jacoby, Esquire

Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D. C. 20554

In the Matter of	)	
	)	
Beehive Telephone Company, Inc.	)	CC Docket No. 97-237
Beehive Telephone, Inc. Nevada	)	
	)	
Tariff F.C.C. No. 1	)	Transmittal No. 6

To: The Commission

PETITION FOR RECONSIDERATION

Beehive Telephone Company, Inc. and Beehive Telephone, Inc. Nevada (collectively "Beehive"), by their attorney, and pursuant to section 405(a) of the Communications Act of 1934, as amended ("Act") and section 1.106(b)(1) of the Commission's Rules ("Rules"), hereby requests the Commission to reconsider its *Memorandum Opinion and Order*, FCC 98-1 (Jan. 6, 1998) ("*Order*") in the above-captioned proceeding. As a party to the proceeding, Beehive has standing to seek reconsideration. *See* 47 U.S.C. § 405(a); 47 C.F.R. § 1.106(a)(2).

Introduction

The *Order* concluded the investigation of the Common Carrier Bureau ("Bureau") of Beehive's 1997 biennial access tariff filing, which was made on a streamlined basis under section 204(a)(3) of the Act, 47 U.S.C. § 204(a)(3). *See generally Implementation of Section 402(b)(1)(A) of the Telecommunications Act of 1996*, 12 FCC Rcd 2170 (1997) ("*Streamlined Tariff Rules*"). Unfortunately, the Bureau's conduct of the investigation did not afford Beehive the full opportunity for hearing required by section 205 of the Act, 47 U.S.C. § 205(a), section 4 of the Administrative Procedure Act ("APA"), 5 U.S.C. § 553, and the Due Process Clause of the Fifth Amendment.

Argument

I. The Bureau's Procedures Deprived Beehive Of Its Statutory Right To A Full Hearing

The Commission has chosen not to promulgate procedural rules to govern tariff investigations. Rather, it has opted to allow the Bureau to formulate procedures on a case-by-case basis. *See Streamlined Tariff Rules*, 12 FCC Rcd at 2220. Nevertheless, tariff investigations are at least rule makings of particular applicability to the named carriers. 1/ Therefore, in addition to complying with the "full hearing" requirement of section 204 of the Act, 47 U.S.C. § 204(a)(1), the Commission must conduct tariff investigations in accordance with the procedural requirements applicable to rule makings under the APA. *See AT&T Co.* v. *FCC*, 572 F.2d 17, 21-23 (2d Cir.), *cert. denied*, 439 U.S. 875 (1978).

The Bureau elected to conduct its investigation of Beehive's local switching rates as a "notice and comment proceeding". *Beehive Telephone Co., Inc.*, DA 97-2537 at 5 (Dec. 2, 1997) ("*Designation Order*"). Consequently, it had to tailor procedures for the investigation that satisfied the notice and comment requirements of section 4 of the APA, 5 U.S.C. 533.

To comply with section 204(a), the Bureau had to allow Beehive and the other interested parties to "meaningfully participate" in the proceeding without "unduly burden[ing]" the Commission's ability

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1/ *See Southwestern Bell Telephone Co.*, 6 FCC Rcd 3760, 3766 (1991); *Investigation of Special Access Tariffs of Local Exchange Carriers*, 5 FCC Rcd 4861, 4861 (1990). *See generally ABC, Inc.* v. *FCC*, 682 F.2d 25, 31-32 (2d Cir. 1982).

to complete the investigation by its January 6, 1998 statutory deadline. *Beehive Telephone Co., Inc.*, DA 97-2597, at 2 (Competitive Pricing Div. Dec. 12, 1997). Therefore, it had to give the parties a "reasonable amount of time" to plead their cases, while leaving the Commission "adequate time" to consider their filings. *Id.* The Bureau had similar obligations under section 4 of the APA, which required it to provide notice of the issues to be investigated and give adequate time "to permit interested parties to comment meaningfully." *Florida Power & Light Co.* v. *United States*, 846 F.2d 765, 771 (D.C. Cir. 1988), *cert. denied*, 490 U.S. 1045 (1989).

Finally, the Commission had the duty to proceed to conclude the tariff investigation "[w]ith due regard for the convenience and necessity of the parties or their representatives and within a reasonable time". 5 U.S.C. § 555(b). Unfortunately, the Bureau proceeded at an inconvenient and unreasonable pace. That led directly to the errors that now taint the decision-making process in this case.

A. Beehive Was Given Inadequate Time To Present Its Case

The Commission was given five months to issue a final order concluding the investigation of Beehive's local switching rates. *See* 47 U.S.C. § 204(a)(2)(A). For no apparent reason, the Bureau took nearly four of those months (from August 5, 1997 to December 2, 1997) just to decide on the issue to be investigated. 2/

2/ *See Beehive Telephone Co., Inc.*, DA 97-1674, at 1 (Com Car. Bur. Aug. 5, 1997) ("*Suspension Order*"); *Designation Order* at 1.

In its last-minute *Designation Order*, the Bureau announced a filing schedule that gave the parties twenty-seven days to file papers and left the Commission eight days to decide the matter. One of those days was lost when the *Designation Order* was not released until December 3, 1997. To make matters worse, the Bureau's schedule called for the parties to meet tight deadlines during the holiday season, clearly the most inconvenient time of the year.

The Bureau did not give Beehive explicit notice of its deadline for submitting its direct case. The "filing schedule" that appeared in the caption of the *Designation Order* indicated that the deadline was December 12, 1997 -- nine days after the order was actually released. *Designation Order* at 1. But the filing schedule set out in Part IV of the order called for Beehive to file a direct case within fifteen days after the release of the order. *See id.* at 5 (¶ 9). The third ordering clause explicitly directed Beehive to meet the same deadline. *See id.* (¶ 15). Obviously, the Bureau's announced schedule was subject to different interpretations.

Beehive reasonably concluded that it was subject to the fifteen-day deadline specified in the Bureau's ordering clauses, because the Commission's filing deadlines are triggered by an "order" as opposed to the accompanying memorandum opinion. *See Microwave Communications, Inc.* v. *FCC*, 515 F.2d 385, 388 & n.8 (D.C. Cir. 1974). Moreover, a nine-day filing period was considered inadequate and inconsistent with the Bureau's normal practice. Nine days was less than a third of the time the Bureau allowed for the

preparation of direct cases in past access tariff investigations. 3/ Therefore, Beehive instructed its consultants that the deadline was December 18, 1997, and they arranged their work schedule accordingly.

It took the Bureau five days to "correct" the *Designation Order*. It issued an erratum to the order on December 8, 1997, which specified December 12, 1997 as Beehive's direct case deadline. Thus, Beehive learned that it only had four more days to complete its direct case.

Since it was working to meet a fifteen-day deadline, Beehive was not prepared to compile all the data necessary to complete its direct case by December 12, 1997. Despite the fact that the Bureau extended the deadline by one business day, Beehive was unable to file a complete direct case on the due date.

Beehive ultimately was given twelve days to present its case, which was less than the comment period that barely withstood challenge in *Omnipoint Corp.* v. *FCC*, 78 F.3d 620, 629-30 (D.C. Cir. 1996). 4/ More significantly, the Bureau's treatment of Beehive was substantially different than the treatment accorded the other

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3/ *See 1993 Annual Access Tariff Filings*, 8 FCC Rcd 4960, 4973 (Com. Car. Bur. 1993) (34 days); *1992 Annual Access Tariff Filings*, 7 FCC Rcd 4731, 4756 (Com. Car. Bur. 1992) (35 days); *Annual 1990 Access Tariff Filings*, 5 FCC Rcd 4177, 4231 (Com. Car. Bur. 1990) (25 days).

4/ In *Omnipoint*, there was good cause for a shortened comment period (effectively fourteen days), including a change in law on the eve of an auction deadline. *See* 78 F.3d at 627. Here, the need for expedition was entirely of the Bureau's own making -- it took too long to issue the *Designation Order*.

local exchange carriers ("LECs") whose 1997 access tariff filings were under investigation. Those LECs were given 30 days to file their direct cases. *See 1997 Annual Access Tariff Filings*, DA 97-1609, at 35 (Com. Car. Bur. July 28, 1997). *See also Tariffs Implementing Access Charge Reform*, DA 98-151, at 39 (Com. Car. Bur. Jan. 28, 1998).

The Bureau's practice in access tariff investigations evidences its recognition that it takes even the largest LECs approximately thirty days to prepare a direct case. The task is at least as difficult for the small carriers such as Beehive, which only has twenty-two employees. 5/ Thus, the twelve days given Beehive was clearly inadequate, especially considering Beehive's detrimental reliance on the schedule originally ordered by the Bureau.

With only an eight-day window between the submission of Beehive's rebuttal (December 29, 1997) and the Commission's deadline to decide the matter, the staff lacked the time to follow its normal practices in "permit-but-disclose" tariff investigations. One such practice is to "engage in discussions for the purpose of obtaining information deemed essential to resolve expeditiously the issues raised in the investigation." *See Beehive Telephone, Inc.* v. *The Bell Operating Companies*, 12 FCC Rcd 17930, 17943 (1997). In tariff investigations, carriers often submit additional information to

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5/ The Commission recognizes that tariff regulation imposes a greater burden on small LECs. That is why the Commission does not require small carriers to submit supporting data with their access tariff filings. *See* 47 C.F.R. § 61.39(b); *Streamlined Tariff Rules*, 12 FCC Rcd at 2234.

justify their rates after the pleading cycle ends. *See, e.g., Local Exchange Carrier Line Information Database*, 8 FCC Rcd 7130, 7132 & n.25, 7147 (1993). Had sufficient time been available, the staff could have requested the specific data deemed necessary for a ruling on Beehive's operating expenses.

Lacking time to allow Beehive to try to justify its actual operating expenses, the staff conducted a study to arrive at a "reasonable estimate" of Beehive's expenses. *Order* at 7. Hence, Beehive was deprived of a chance to supply the data the staff felt was missing.

A carrier should be given an ample opportunity to carry its burden of proof in a tariff investigation. *See LECs' Rates, Terms and Conditions for Expanded Interconnection Through Physical Collocation for Special Access and Switched Transport*, 8 Com. Reg. (P&F) 524, 624 (1997). Beehive did not get that opportunity in the abbreviated investigation in this case.

B. Beehive Was Not Given The Opportunity To Comment On The Bureau Study

Under section 205(a) of the Act, rates can be prescribed only "after full opportunity for hearing". 47 U.S.C. § 205(a). That means that a carrier must be given a "'full opportunity' to be heard", *AT&T Co.* v. *FCC*, 572 F.2d 17, 22 (2d Cir.), *cert. denied*, 439 U.S. 875 (1978), in a "type of hearing appropriate in the particular case", *Western Union Telegraph Co.* v. *FCC*, 665 F.2d 1126, 1151 (D.C. Cir. 1981). Because the rate prescription applies only to Beehive, the investigation in this case was equivalent to

adjudication. Therefore, Beehive was entitled to notice of the case against it and the opportunity for rebuttal.

The Commission based its decision on Beehive's perceived failure to supply an "adequate explanation" for the increases in its operating costs in 1995 and 1996. *Order* at 6. However, Beehive was not given the opportunity to further explain its actual operating expenses. Instead, the Commission proceeded to estimate Beehive's operating expenses. *See id.* at Appendix.

The Commission estimated that Beehive's expenses totalled $2,819,404 in 1995 and 1996. *See id.* That estimate was the conclusion of an unpublished staff study of "unseparated data" filed with NECA by 55 unidentified LECs serving between 800 and 1000 access lines in 1995 or 1996. *Id.* at 7. The data collected by the staff is not in the record and was not provided to Beehive. Because the study was first disclosed with the *Order*, Beehive had no opportunity to comment on the methodology or results of the study before it became the basis of the Commission's decision.

Section 4 of the APA is violated when the Commission "use[s] critical, yet unpublished, data to reach its conclusions". *National Black Media Coalition* v. *FCC*, 791 F.2d 1016, 1024 (2nd Cir. 1986). Thus, the Commission committed a "serious procedural error" when it failed to reveal the staff's study in time to allow for "meaningful commentary". *Connecticut Light and Power Co.* v. *NRC*, 673 F.2d 525, 531 (D.C. Cir.), *cert. denied*, 459 U.S. 835 (1982). It must reconsider its decision after it allows Beehive to comment on the Bureau's methodology, data and calculations. *See Idaho Farm Bureau*

Federation v. *Babbitt*, 58 F.3d 1392, 1403-4 (9th Cir. 1995); *Solite Corp.* v. *EPA*, 952 F.2d 473, 499-500 (D.C. Cir. 1991).

II. The Commission Violated Beehive's Fifth Amendment Rights

The Commission prescribed for Beehive a premium local switching rate of $0.009443 per minute of use and a non-premium local switching rate of $0.004249. *Order* at 10. It also directed Beehive to make refunds for the period of August 6, 1997 through December 31, 1997, with interest. *Id.* at 11. In compliance with that directive, Beehive is issuing refunds totalling $140,915.56 to its customers.

The Commission's rate prescription and refund order directly implicated Beehive's property interests protected by the Due Process and Takings Clauses of the Fifth Amendment. *See Duquesne Light Co.* v. *Barasch*, 488 U.S. 299, 307-8 (1989). Beehive had a constitutional right to procedural due process before it could be ordered to refund previously collected rate charges. *See Ohio Bell Telephone Co.* v. *Public Utilities Commission of Ohio*, 301 U.S. 292, 304-6 (1937). The Fifth Amendment also protected Beehive from being required to charge rates that do not afford it "sufficient compensation". *Duquesne*, 488 U.S. at 308.

The Commission's refund order was a "quasi-judicial" determination, *United States* v. *Florida East Coast Railway Co.*, 410 U.S. 224, 245 (1973), which could not, consistent with due process, be made on the basis of undisclosed evidence that was never made part of the record, *see Ohio Bell*, 301 U.S. at 304-6. Thus, the Commission vio-

lated the Fifth Amendment, as well as section 4 of the APA, when it used an off-the-record study to prescribe rates for Beehive.

The Commission erred when it claimed authority, under the *Permian Basin Area Rate Cases*, 390 U.S. 747 (1968), to prescribe rates for Beehive based on a "cost-averaging methodology". *See Order* at 8. The Supreme Court held in *Permian Basin* that agencies have the discretion, within constitutional and statutory limitations, to respond to the changing characteristics of a regulated industry by adopting new ratemaking methodologies for a "regulated class". *See* 390 U.S. at 768-77. *See also Duquesne*, 488 U.S. at 313-14. The Court did not hold that an agency can depart from established ratemaking principles to prescribe rates for a single carrier in a quasi-adjudicative proceeding. 6/ Nor did it hold that any system of ratemaking by an agency will necessarily be constitutional. *See Duquesne*, 488 U.S. at 314.

Prescribed rates must be calculated in conformity with the pertinent constitutional limitations. *Permian Basin*, 390 U.S. at 769. Agency ratemaking is "unconstitutional . . . if arbitrary,

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6/ Beehive does not dispute that the Commission may establish a generic ratemaking methodology in a rulemaking of general applicability. Beehive also does not contest that the Commission may adopt a "cost-averaging methodology" to be applied prospectively to an entire regulated industry segment. That is what the Commission did in the rulemaking proceedings it cited in its *Order*. *See Price Cap Performance Review for LECs*, 10 FCC Rcd 8961 (1995); *Simplification of the Depreciation Prescription Process*, 8 FCC Rcd 8025 (1993); *Represcribing the Authorized Rate of Return for Interstate Services of LECs*, 5 FCC Rcd 7507 (1990); *Policy and Rules Concerning Rates for Dominant Carriers*, 5 FCC Rcd 6786 (1990). However, the Commission cannot announce and apply a new cost-averaging methodology in its final order in a one-carrier tariff investigation.

discriminatory or demonstrably irrelevant to the policy the legislature is free to adopt". *Permian Basin*, 390 U.S. at 770 (quoting *Nebbia* v. *New York*, 291 U.S. 502, 539 (1934)). Thus, a ratesetting agency cannot "arbitrarily switch back and forth between methodologies" without raising "serious constitutional questions". *Duquesne*, 488 U.S. at 315. Beehive submits that the Commission exceeded its constitutional limitation when it switched from its ratemaking rules to fashion a *sui generis* methodology in this case.

The Commission recognized that the methodology for developing Beehive's local switching rates is prescribed by section 61.39(b)(1)(ii) of the Rules. *See Designation Order* at 3 & n.19. Under that methodology, rates are developed from the company's "actual historical costs". *Regulatory Reform for LECs Subject to Rate of Return Regulation*, 8 FCC Rcd 4545, 4558 (1993). *See Regulation of Small Telephone Companies*, 2 FCC Rcd 3811, 3812-13 (1987). The Commission was bound to follow section 61.39(b)(1)(ii) until such time as it altered that rule through a rulemaking. *Southwestern Bell Telephone Co.* v. *FCC*, 28 F.3d 165, 169 (D.C. Cir. 1994). By concocting its new "average ratio of operating expenses to gross investment" methodology in this case, *Order* at 7, the Commission arbitrarily departed from its own rule. *See Southwestern Bell*, 28 F.3d at 167.

Beehive had a cognizable property interest in retaining the charges it collected for the use of its utility property. The Commission infringed on that protected interest by subjecting Beehive to an arbitrary ratemaking methodology with no notice or oppor-

tunity to be heard. By singling Beehive out for such treatment, the Commission violated both the Due Process Clause of the Fifth Amendment and the implied equal protection guarantee of that clause.

III. The Commission Must Remedy Its Procedural Errors By Reopening The Record

Beehive's request for reconsideration of the *Order* rests in large part on facts not previously presented to the Commission. Nevertheless, consideration of those facts is warranted by law and the public interest.

The appropriate remedy for a violation of the notice and comment provisions of the APA is for the Commission to reconsider the matter "[o]n a more developed record". *MCI Telecommunications Corp.* v. *FCC*, 57 F.3d 1136, 1143 (D.C. Cir. 1993). Consideration of facts not "previously presented" in such a case, *see* 47 C.F.R. § 1.106(c), should be considered because the party previously had been given an inadequate "opportunity to present such matters", *see* 47 C.F.R. § 1.106(b)(2)(i). Thus, the additional cost and demand information proffered by Beehive falls within the categories of new facts that can be considered on reconsideration. *See* 47 C.F.R. § 1.106(c)(1).

The Bureau's failure to give explicit notice of the direct case deadline in this case contributed to Beehive's inability to present all its cost and demand data earlier. The Commission should not allow Beehive to be prejudiced because of "a lack of notice attributable to a procedural omission by the Bureau". *Central Mobile Radio Phone Service*, 65 FCC 2d 648, 651 (1977). Both admini-

strative fairness and the public interest would be served if the Commission reopens the record to give Beehive a "full opportunity to be heard".

In any event, the facts offered in rebuttal to the staff's study of the NECA data must be considered. First, the study itself constitutes a "changed" circumstance within the meaning of section 1.106(c) of the Rules. The study was decisionally significant and was first disclosed after Beehive had its "last opportunity" to present facts. 47 C.F.R. § 1.106(b)(2)(i). Moreover, Beehive was entitled to a fair opportunity to comment on the "key study" in this case, and the Commission's failure to provide that opportunity "may fatally taint the agency's decisional process." *National Association of Regulatory Utility Commissioners* v. *FCC*, 737 F.2d 1095, 1121 (D.C. Cir. 1984), *cert. denied*, 469 U.S. 1227 (1985). That failure can be remedied by allowing Beehive "ample opportunity" to address the Bureau's study now. *See id.*

IV. The Staff's Cost-Averaging Methodology Cannot Be Used To Prescribe Beehive's Rates

The Commission is bound to adhere to its own rules, *e.g.*, *Reuters Ltd.* v. *FCC*, 781 F.2d 946, 950 (D.C. Cir. 1986), and to its announced and established procedures, *Gardner* v. *FCC*, 530 F.2d 1086, 1090 (D.C. Cir. 1976). Therefore, the Commission could not base its rate prescription on the staff's estimate of Beehive's "allowable operating expenses". *Order* at 7. Section 61.39(b)(1)(ii) of the Rules prescribes that Beehive's rates be based on its actual historical costs. *See supra* p. 11. Consequently, the Commission

was obliged to prescribe Beehive's rates "in accordance with [s]ection 61.39." *Designation Order* at 3. 7/

Assuming that it could lawfully prescribe rates on the basis of an unpublished study employing an altogether new methodology, the Commission erred by giving dispositive weight to the staff's study in this case. First, the study was not "based in part on industry's average costs". *Order* at 8. It was based on an "average ratio of operating expenses to gross investment" of fifty-five LECs with comparable number of access lines. *Id.* Moreover, the staff made the invalid assumption that "[a]bsent unusual circumstances, which Beehive has not shown in this record, we would expect Beehive to have a substantially similar ratio of operating expenses to gross investment as other LECs that have a similar operating size." *Id.* at 7.

Beehive was not on notice that it had to show "unusual circumstances" to explain the comparative dissimilarity of its ratio of total operating expenses ("TOE") to total plant in service ("TPIS"). However, that showing is easily made.

Beehive is an unusual telephone company. It was founded in

7/ The Commission designated for investigation the specific issue of whether Beehive's local switching rates were "based on *its* interstate cost of service" for the 1995-96 period. *Designation Order* at 3 (emphasis added). Having taken evidence and heard argument on that issue, the Commission was obliged to resolve it in this case, *see MCI Telecommunications Corp.* v. *FCC*, 917 F.2d 30, 41 (D.C. Cir. 1990), even if that required the adduction of additional evidence. But the Commission could not decide the designated issue on the basis of an *ad hoc* departure from the ratesetting methodology prescribed by its own rule.

1965 by Arthur W. Brothers to bring telephones to Utah's unserved areas. For years, Mr. Brothers served as a one-man telephone company (he hired his first full-time employee in 1980). He brought telephone service to remote and sparsely-populated areas using surplus equipment (often by draping old military communications cables along roadside barbed-wire fences). In its first twenty years, Beehive never turned a profit, and Mr. Brothers never drew more than $5,000 a year from the company. 8/

Beehive's operating environment differs dramatically from most of the small LECs that serve between 800 and 1,000 access lines. Beehive's subscribers are in tiny villages scattered throughout parts of seven Utah counties and two counties in Nevada. Its combined service area consists of eight widely dispersed and sparsely populated areas in two states. *See infra* Exhibit 2. To serve its 882 access lines, Beehive currently operates fourteen exchanges and uses a total of 1,180 route miles of cable. *See infra* Exhibit 3. Thus, Beehive only serves an average of 63 access lines per exchange and less than one access line (0.75) per route mile of cable. That makes Beehive a very high cost LEC.

Beehive compared its operations with thirty-seven other LECs which serve between 800 and 1,000 access lines as reported by the

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8/ The efforts of Mr. Brothers to provide telephone service to remote areas no other company would serve has been recognized in the national media since the early 1980s. *See infra* Exhibit 1 (Kathryn Christensen, *In Utah Hinderlands, 'An Old Westerner' Is Talk Of The Towns*, Wall St. J., Jan. 6, 1981). Mr. Brothers was the subject of the NBC feature "In Pursuit of the American Dream" which aired on the Today Show on January 14, 1982.

Rural Utilities Service ("RUS") of the United States Department of Agriculture. 9/ The 1996 RUS data showed that Beehive is among the lowest density LECs in terms of access lines per exchange and per mile. *See infra* Exhibit 4 at 2. Beehive has more exchanges (14) than the nearest similarly sized LEC (9). Only one of the thirty-seven small LECs served fewer access lines per route mile than Beehive. *See id.* The following shows how Beehive compares to the average number of exchanges, lines per exchange, and lines per route mile of the other small LECs.

	Beehive	37 LECs
Exchanges	14	2.03
Access Lines Per Exchange	63	450.65
Access Lines Per Route Mile	0.75	5.25

The foregoing analysis suggests that Beehive may be unique among LECs within the Commission's 800-1,000 access line benchmark. Considering the low density of access lines per route mile and per exchanges, Beehive's operating expenses predictably would be higher than most other high cost-per-loop LECs.

Beehive has used NECA's Universal Service Fund ("USF") database to compile a list of the LECs with the highest TOE to TPIS ratios. *See infra* Exhibit 4 at 2. It also sorted the NECA USF database on the basis of TPIS per loop and TOE per loop. *See id.* at 3-4. The data confirms that Beehive's TOE to TPIS ratio (50.13%) and its TOE

9/ *See* Rural Utilities Service, United States Department of Agriculture, *1996 Statistical Report Rural Telecommunications Borrowers* (Informational Publication 300-4).

per loop ($3,489) are comparatively high, while its TPIS per loop ($6,959) is low among the sample group. However, Beehive's TOE to TPIS anomaly is explained by the fact that it uses leased switching equipment at four of its exchanges.

Beehive's central office expenses include approximately $28,000 per month in operating lease expense associated with switches deployed in its exchanges. This switch leasing cost is booked as an operating expense rather than as an investment in the TPIS switching account. This choice results in Beehive's expenses being greater, and its TPIS account being lower, than it otherwise would have been. If the switching functionality was purchased and booked as an investment rather than leased, the $28,000 monthly expense would represent the equivalent capital cost of a switching investment of approximately $1.4 million as demonstrated below:

Line		
1	Investment	$1,397,350
2	Depreciation	0.07
3	Rate of Return	0.1125
4	FIT Gross Up	1.515151
5	Total Monthly Capital Cost L.1 x (L.2 + (L.3 x L.4))/12	$28,000

If the data is restated to reflect the acquisition of a switching asset, Beehive's TOE would decrease by $336,000, while its TPIS would increase by $1,397,351. Beehive's TOE to TPIS ratio would be reduced from 50.01% to 36.71%, and its rank among the sample LECs would drop from 12th to 39th. *See infra* Exhibit 4 at 5.

The staff's effort to estimate Beehive's operating expenses as a percentage of its TPIS is flawed in two basic respects. First, due to its extraordinary low subscriber density, Beehive is not just a "higher than average cost carrier". *Order* at 7. Second, the staff's analysis penalizes Beehive for its operating lease method of asset acquisition.

Even if it arrived at a reasonable estimate of Beehive's operating expenses, the staff erred when it calculated demand for the purposes of developing Beehive's local switching rates. First, it erroneously found that the dial equipment minutes ("DEMs") reported in Beehive's direct case differed from the DEMs reported in its rebuttal. *See Order* at 10. However, Beehive did not report its total DEMs in its rebuttal case -- it gave its total 1995/96 "access minutes" (55,585,464). Beehive reported its total 1995/96 DEMs (59,484,566) in its direct case. *See infra* Exhibit 5.

Due to the misperceived discrepancy in the DEMs reported, the staff used Beehive's total DEMs of 59,484,566 to determine demand. *See Order* at 10. In contrast, Beehive utilized its DEMs to allocate local switching equipment costs between the interstate and intra-state jurisdictions. *See* 47 C.F.R. § 36.125(b). It used its 1995/96 premium (31,407,602) and non-premium (24,177,862) access minutes to develop its rates. *See infra* Exhibit 5. That was the correct methodology, because Beehive was required to base its local switching rates on "related demand for calendar years 1995 and 1996". *Designation Order* at 3. *See* 47 C.F.R. § 61.39(b)(1)(ii). The weighted DEMs would not reflect Beehive's actual 1995/96 demand.

V. Beehive's 1995/96 Expenses Should Be Allowed

The Commission ruled that Beehive failed to provide an adequate explanation for the "dramatic increase" in its plant specific and corporate operations expenses. *Order* at 5-6. Beehive's plant specific expenses totalled $354,813 in 1994, $1,454,405 in 1995, and $1,227,761 in 1996. Its corporate operating expenses were $675,429 in 1994, $1,614,323 in 1995, and $1,297,484 in 1996.

Beehive began leasing switch equipment in 1995, which caused the dramatic increase in its plant specific expenses. Lease costs totalled $796,074 in 1995, but dropped to $672,000 in 1996. Additional switch equipment was leased in 1995 in order to meet the increased usage generated by Beehive's arrangement with Joy Enterprises, Inc. ("JEI").

The increase in corporate operations expenses was attributable primarily to extraordinary litigation costs and increased administrative expenses attendant to Beehive's efforts to stimulate traffic on its system. Beehive incurred legal and accounting costs of $557,236 in 1994, $954,594 in 1995 (when Beehive was a party to state and federal law suits, as well as litigation before the Commission), and $457,520 in 1996. During this period, Beehive's administrative costs increased from $63,070 in 1994 to $583,581 in 1995 to $767,626 in 1996.

In October 1994, Beehive entered into its arrangement with JEI to provide conference bridge services, including a chat line. The arrangement was intended to generate sufficient revenues so that

Beehive could continue to operate exchanges in remote locations (one of which is accessible by water only) and to provide telephone service to a vast, sparsely populated area without the aid of state and federal subsidies. 10/ Beehive's goal was to increase its minutes of use in order to reduce its unit cost and lower its 1994 $.47 per minute access rate. Because of the increased traffic generated by the JEI arrangement, Beehive has been able to drastically reduce its access charges as depicted below:

Switched Access Service	1994 ($)	1995 ($)	1997 ($)
Premium Local Transport Facility Per Access Minute Per Mile	0.00358	0.00127	0.00066
Premium Local Transport Termination Per Access Minute	0.1470	0.04768	0.01815
Non-Premium Local Transport Facility Per Access Minute Per Mile	0.00161	0.00054	0.000299
Non-Premium Local Transport Termination Per Access Minute	0.0662	0.02142	0.00817
Premium Local Switching Per Access Minute	0.1540	0.03480	0.04012
Non-Premium Local Switching Per Access Minute	0.0693	0.01566	0.01805

Beehive's arrangement with JEI is not unusual. It is common within the telecommunications industry for carriers to enter into agreements to stimulate traffic. *See International Audiotext*

10/ For Mr. Brothers description of the difficulties attendant to Beehive's operations, *see infra* Exhibit 6 (Comments from Beehive Telephone Companies, CC Docket No. 96-45 (Jan. 26, 1998)).

Network, Inc. v. *AT&T Co.*, 893 F.Supp. 1207 (S.D.N.Y. 1994), *aff'd*, 62 F.3d 69 (2d Cir. 1995). Moreover, costs incurred by carriers to stimulate usage have been recognized by the Commission as legitimate business expenses. *See AT&T's Private Payphone Commission Plan*, 3 FCC Rcd 5834, 5836 (Com. Car. Bur. 1988), *rev. denied*, 7 FCC Rcd 7135 (1992). *See also International Telecharge, Inc.* v. *AT&T Co.*, 8 FCC Rcd 7304, 7306 (Com. Car. Bur. 1993); *National Telephone Services*, 8 FCC Rcd 654, 655 (Com. Car. Bur. 1993). Beehive's expenses should also be deemed legitimate and allowable.

The expenses Beehive incurred to stimulate traffic were reasonably related to local switching service, because they increased the use of that service and decreased costs to Beehive's customers. For example, in 1994 Beehive's per minute premium access charge for one mile of transport was $.30458. Under Beehive's 1997 tariff rates, that charge had dropped to $.05893. Similarly, Beehive's non-premium charge dropped from $.13711 to $.02659. Thus, Beehive's interexchange carrier customers benefited from increased usage at lower access costs.

Beehive's local subscribers and their communities have also been benefited. Beehive has been able to maintain its local service at low rates. *See infra* Exhibit 6 at 2. The public interest in maintaining telephone service to remote areas is obvious. 11/ Beehive's operating expenses should therefore be allowed.

11/ *See infra* Exhibit 7 (Fred Vogelstein, *A Really Big Disconnect*, U.S. News & World Reports at 39 (Feb. 2, 1998)).

VI. Beehive Did Not Use An Unauthorized Rate Of Return

The Commission made the finding that Beehive "use[d] an unauthorized rate of return in calculating the interstate local switching rates contained in Transmittal No. 6". *Order* at 7. That finding was erroneous and should be changed.

Beehive used the prescribed rate of return of 11.25% when it developed its rates in June 1997. 12/ The rates of return reported in Beehive's direct case for local switching in 1994, 1995 and 1996 reflect what Beehive actually earned for that service category. Thus, there is no basis to find that Beehive targeted an unlawful rate of return.

For all the foregoing reasons, Beehive respectfully requests that the Commission reconsider its *Order*.

Respectfully submitted,

BEEHIVE TELEPHONE COMPANY, INC.
BEEHIVE TELEPHONE, INC. NEVADA

By /s/ Russell D. Lukas
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12/ *See* Letter of Russell D. Lukas to James D. Schlicting (Aug. 27, 1997) (transmitting Beehive's 1996 toll cost study supporting Transmittal No. 6).

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In Utah Hinterlands, 'An Old Westerner' Is Talk of the Towns

* * *

Arthur Brothers, 50, Brings Phones to Neglected Areas, Dismay to Bureaucracies

By Kathryn Christensen
Staff Reporter of The Wall Street Journal

GROUSE CREEK, Utah — By rancher Winfred Kimber's reckoning, it wasn't until about 1965 that modern civilization came to this remote village in Utah's northwestern corner, and then it came *in* the unlikely form of one "strange but brilliant man" by the name of Arthur W. Brothers.

"He did what nobody else would: He brought us telephones," Mr. Kimber says with admiration. "He built it little by little like a poor man, but he got it done."

In the nearly 50 years since the community's only telegraph linkup went to pieces, the few dozen families living here had pleaded with at least four telephone companies to bring service to their area. "None of them wanted us, pure and simple," Mr. Kimber recalls, so he and his neighbors used to drive the 40 miles to Oakley, Idaho, whenever they needed to make a phone call.

That was the first telephone system Mr. Brothers built, and it still has only 36 subscribers. Since 1968, Mr. Brothers, now 50 years old, has been *spending the prime of* his life bringing telephone service to areas of Utah so remote and sparsely populated that no ledger-toting businessman would touch them. For a mere 170 customers—scattered over three sections of land nearly the size of Massachusetts—he has strung miles of wire through mountain passes and draped surplus military communications cable along ranchers' barbed-wire fences. Never, he says, has he made a profit.

Pained Regulators

But it's a mistake to assume that such accomplishments make him beloved by everyone, for Mr. Brothers and his tiny Beehive Telephone Co. are the bane of anything bureaucratic. Regulators groan at the mention of his name—and at his almost-total disregard for their rules and procedures.

"From a regulatory standpoint, dealing with Art in a formal hearing is an ordeal," says Brent Cameron, a Utah public-service commissioner. "Other companies come in with lawyers and cost documents, but Art just comes in by himself." Another commissioner, David Irvine, complains that if everyone operated the way Mr. Brothers does, "it wouldn't be possible for the regulatory system to function."

And even though respecting Mr. Brothers as a "brilliant innovator," the commission's chairman, Milly Bernard, says she often throws him out of her office. "We tell him to shape up," she sighs, "but that's like telling one of your kids to behave."

Mr. Brothers fares even worse with federal authorities.

For starters, the Federal Aviation Administration has never appreciated his habit of landing his small airplane on highways as he barnstorms from one corner of Utah to another repairing his equipment. Because of a *few too-close encounters* with vehicles (including one accident in which a truck passenger was injured), the FAA suspended his pilot's license in 1977 and subsequently revoked it when the agency charged that Mr. Brothers obtained a new license through fraud. Mr. Brothers says a jury recently found that the new license wasn't obtained through fraud, and he is free to fly legally in any case, he has his ad[illegible]ters. "What Art needs is a mother to k[illegible] him on the straight and narrow and a [illegible]ger to handle his public relations." Frederick Foley, a communications e[illegible]neer for the state Public Service Commission. "He isn't

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'An Old Westerner' Brings Phones To Rural Utah, Dismay to Agencies

Continued From First Page

a conventional operator, and he does take some liberties, but you've got to give the devil his due. Art Brothers is the only one who is going to supply service for some of these people. Who else would take on these mostly Godforsaken areas and put together a telephone system?"

Air Force Training

Even Mr. Brothers can't answer that, for he himself isn't quite sure why he got into the telephone business. His only training, he says, came during his four years as an Air Force radar and radio specialist. After his discharge, he used the GI bill to study business management at the University of Utah, then took off for New York to work for a technical magazine.

Later, he moved to California and subsequently back to Utah as a manufacturer's representative for communications companies. Then, an acquaintance proposed forming a partnership to start a company that would bring telephones to Utah's unserved areas. The acquaintance backed out at the last moment, but Mr. Brothers proceeded. He named his enterprise Beehive Telephone Co. after Utah's symbol of (busy) industry.

"I guess that once I got started, I just wanted *to prove to somebody* I could do what I said," he theorizes now. To raise capital for Beehive, he asked for $50 "aid-to-construction" payments from customers, the same fee he charges for installations. (His basic monthly charge is $12.50, identical to that of other Utah telephone companies.)

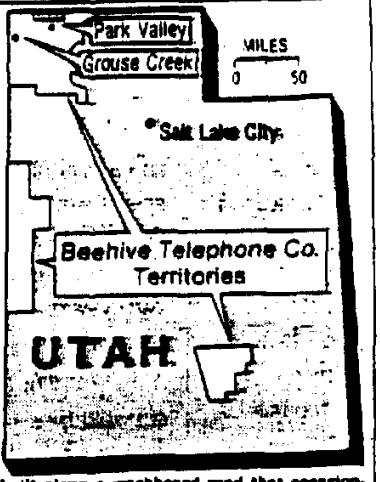
"The only thing I put into this business was my time and hard work," Mr. Brothers says. "I went to other companies and took their scrap and surplus wire, and I rebuilt old switching units. Anything that cost money, I tried to trade (Beehive) stock for." Not until last year did he hire a full-time employe. Previously, he relied on his three children and friends to help him with whatever construction work couldn't be done by one man.

No Soft Life

But for anyone with a similar yen to build and own an independent telephone company, Mr. Brothers has a warning: It's no cushy life of emptying overflowing coin boxes or letting your fingers do the walking. In a recent seven-day stint, Mr. Brothers drove more than 1,200 miles, heaved telephone poles on the trailer behind his pickup truck, climbed other poles to repair wires, installed telephones and firmly—but diplomatically—called on customers who haven't paid their bills or whose checks have bounced.

Here in his northwestern territory, where Beehive has 36 telephones in Grouse Creek and 36 in Park Valley, Mr. Brothers and his one employe, James Ball, spent nearly an entire day burying 1,200 feet of telephone cable so a rancher might get a telephone before Christmas. Snow was falling, and the ground was so hard and rocky that their small cable plow moved at a maddening creep. The two men stopped working only long enough to make a dry sandwich from the supplies that Mr. Brothers carries in a cooler and to wash it down with his ever-present jug of milk.

In 1979, Mr. Brothers received a $100,000 Small Business Administration loan to upgrade his service here, and he is gradually retiring some of the old military communications cables still looped through roadside fences. The improvement is needed. Mr. Brothers says he is looking forward to a time when this system won't be vulnerable to cattle stumbling through cables and dis-



built along a washboard road that occasionally crosses the original Pony Express trail.

Driving and politicking through that territory, Mr. Brothers knocks on doors of houses and schools and urges whoever appears to write his Congressman about speeding up that loan. "We'll do it," promises Nick Zakis of Gold Hill. "We can sure use those phones." Others are equally cooperative. Like Mr. Brothers, they believe their chances of getting telephone service are better now than ever, largely because the MX missile system might be located here and bring demanding government workers to the area.

Hope for a Profit

Such a possibility brings a gleam to Mr. Brothers's eyes. His telephone company, the smallest in Utah, has yet to make a profit, though Mr. Brothers says he would have broken into the black a couple of years ago had it not been for expenses that the company has incurred "fighting the bureaucracy." Beehive's annual losses have never exceeded $7,000, he says, adding that last year he drew about $4,200 out of Beehive's $70,000 in revenue.

Mr. Brothers says he has never drawn more than $5,000 a year from Beehive. He explains that a small sum has been enough because his Salt Lake City home was paid for before he founded the company and because "I don't spend much money." Indeed, he is something of a thrift fanatic. For example, his wardrobe centers around several dozen pairs of pants he bought for 60 cents each, and his stationery consists of the backs of letters he has received from others.

"He doesn't know what it means to go out to dinner or buy something new," says Ben Schafer, a friend who occasionally works with Mr. Brothers. And Mr. Brothers himself acknowledges that he has few friends and almost no social life.

"Art has been running a strictly hand-to-mouth operation with war-surplus materials and anything else he can scrounge up; he's the king of recyclers," says Mr. Foley of the public-service commission. "Now it looks like he might make some money, what with the MX thing and Ticaboo."

Ticaboo, a two-year-old uranium boom town in the state's southeastern corner, is Mr. Brothers's third and newest territory. *The town itself is no more than a motel*, a grocery store and a cluster of some 400 house trailers belonging to the miners and construction workers. Huge rock and clay mesas jutting out of the raggedy, tumbleweed terrain give the countryside a look of hardness, but Art Brothers thinks the view is grand.

Brand-New Gear